

General Fund Balancing Strategy Detail

INTRODUCTION

This General Fund Balancing Strategy Detail Attachment is intended to provide a brief, but more detailed summary of the key actions provided for in the General Fund as part of the overall strategy to balance the 2005-2006 Adopted Operating Budget. Specifically, by each stage of the process, both significant revisions to the original February 2005 General Fund Forecast Base Budget, as well as the key elements of the strategy to bring the General Fund into balance in the Adopted Budget are described.

In February 2005, the Administration presented to the City Council formal projections for the 2005-2006 General Fund budget as part of the *2005-2006 City Manager's Budget Request & 2006-2010 Five-Year Forecast and Revenue Projections* document. The 2005-2006 "base-case" projections in that document indicated the presence of a shortfall totaling approximately \$56.9 million. This "shortfall" represented the difference or gap between projected 2005-2006 General Fund resources and the expected cost of both current services in next year's terms, and providing for several City Council committed augmentations (such as the costs of operating and maintaining new facilities).

In addition to the basic projected shortfall in the General Fund of \$56.9 million, it was noted that an additional shortfall of about \$0.8 million existed in the cost-recovery, development-related fee programs in the General Fund.

Subsequent to the release of the February Forecast, a number of changes to both expenditures and revenue estimates were made, when combined, constituted the Revised Forecast Base Budget included in the

Proposed Budget. These revisions reflected the most current information about economic conditions and cost/activity projections.

Discussed in more detail below, the revisions to the Base Budget included a series of changes that produced a net addition in General Fund sources of \$4.3 million, and an increase in overall costs of \$4.6 million. The combined impact of these changes to the Base Budget increased the basic estimated shortfall in the General Fund to be closed in the Proposed Budget only slightly, by \$0.35 million, to the \$57.24 million amount that was addressed by our budget balancing plan. The revenue and expenditure adjustments to the Base Budget are described in more detail below.

In addition to developing a strategy to eliminate the basic \$57.24 million shortfall, a separate strategy was approved to address the additional small shortfall (gap) (\$0.81 million), which was projected for the General Fund cost recovery development fee programs. In order to isolate the fee program problem and ensure that solutions were made specific to those fee programs, that gap was listed and discussed separately from the basic General Fund shortfall. The development fee programs are directed by City Council policy to recover 100% of the cost of development review and inspection. The February Forecast assumed that these fee programs would develop a strategy that would completely address its shortfall. The Adopted Budget included such a strategy.

The following Table I displays the overall projections for the 2005-2006 General Fund as they changed between February and the Adopted Budget, the impact of those revisions on the overall Adopted Budget shortfall projections, and the components of

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the balancing strategy. The 2005-2006 Proposed Budget contained solutions that increased sources (including additional Ending Fund Balance dollars created by liquidating several existing reserves) by a total of \$42.09 million, and reduced net costs by \$15.96 million. The net expenditure change was made up of two components: program expenditure reductions of \$27.1 million (which equated to approximately 1.5% of public safety, and 8.2% of non-public safety CSA program budgets), offset by \$11.1 million in proposed augmentations. The result was a balanced 2005-2006 Proposed General Fund Budget of \$745.35 million.

The balancing strategy proposed by the City Manager in this document deliberately contained a combination of ongoing and one-time solutions. Although the one-time solutions would mean that we would almost certainly face a sizeable budget problem again

next year, the use of one-time solutions was kept to what was considered a prudent level, and helped prevent even more dramatic reductions to basic City services. The overall strategy balanced approximately 52% of the total shortfall (including the development fee program impact) with ongoing solutions totaling \$29.9 million. The amount balanced with one-time solutions was \$28.1 million. The specific elements of the Administration's proposed strategy are displayed in Table II, and described in the material that follows.

The 2005-2006 Adopted Budget added additional resources of \$96.3 million, bringing the total budget to \$841.69 million, and included a significant number of revisions to the Proposed Budget. The largest component of the increase was the carrying forward of funds from 2004-2005 for the completion of various projects. These changes are summarized in Table III and are described later.

Table I
2005-2006 ADOPTED OPERATING BUDGET
Forecast To Adopted Budget Reconciliation

	Total Sources	Total Uses	(Shortfall)/ Surplus
February Forecast	\$ 698.96	\$ 755.85	(\$ 56.89)
Forecast Revisions	4.30	4.65	(0.35)
Revised Forecast (no fee impact)	703.26	760.50	(57.24)
Development Fee Program Impact	0.00	0.81	(0.81)
Revised Forecast (with fee impact)	703.26	761.31	(58.05)
Proposed Revisions	42.09	(15.96)	58.05
2005-2006 Proposed Budget	\$ 745.35	\$ 745.35	\$ 0.00
Adopted Revisions	96.34	96.34	0.00
2005-2006 Adopted Budget	\$ 841.69	\$ 841.69	\$ 0.00

General Fund Balancing Strategy Detail (Cont'd.)

REVISED FORECAST BASE BUDGET

As discussed above, following the issuance of the February Forecast, detailed analysis of the status of General Fund revenues and expenditures continued. Based on this review, a series of changes to the Forecast Base Budget estimates for both sources and

uses were incorporated into the Proposed Budget in the form of a Revised Forecast. This Revised Forecast Base Budget (no fee impact) resulted in a revised shortfall estimate of \$57.24 million, up only slightly (\$0.35 million) from that shown in the February Forecast.

Revisions to the source estimates contained in the February Forecast that were incorporated into the Revised Forecast included the following:

<u>Sources</u>	<u>Revision</u>
Property Tax	\$ (500,000)
Transient Occupancy Tax	312,000
Licenses & Permits	499,000
Use of Money & Property	(500,000)
Revenue from Local Agencies	(1,268,000)
Departmental Charges	299,000
Other Revenue	(3,022,000)
Transfers and Reimbursements	3,489,000
Beginning Fund Balance	<u>5,000,000</u>
Net Change in Sources	\$ 4,309,000

Use revisions made to the February Forecast Base Budget included:

<u>Uses</u>	<u>Revision</u>
Net Zero Change in treatment of Capital Overhead Functions	\$ 3,019,000
Jail Bookings Fees	(1,266,000)
Net Zero Change in treatment of New City Hall Costs	3,376,000
Miscellaneous Revisions	<u>(474,000)</u>
Net Change in Uses	\$ 4,655,000

General Fund Balancing Strategy Detail (Cont'd.)

REVISED FORECAST BASE BUDGET (CONT'D.)

The revisions to the source estimates presented in February were made to reflect the latest information available. The largest change, a \$5.0 million increase in the estimate for 2004-2005 Ending/2005-2006 Beginning Fund Balance, reflected a recent review of all of the elements of the 2004-2005 budget, including revenue collections and expenditures. As a result of this review, we believed 2004-2005 revenue collections would end the year approximately \$5.0 million higher than forecasted in February. The main components of this change resulted from higher than originally anticipated receipts from Sales Tax, Transient Occupancy Tax, and Telephone Utility Tax.

For 2005-2006, the Property Tax estimate was decreased by \$500,000 based on discussions with Santa Clara County related to SB 813 estimated receipts.

The 2005-2006 Transient Occupancy Tax estimate was increased by \$312,000 based on higher than anticipated performance in the first two quarters of 2004-2005.

The 2005-2006 Licenses and Permits category estimate was increased by \$499,000 reflecting an upward adjustment in the estimates for the Building and Fire Fee Programs and some minor revisions to miscellaneous fees and charges (\$1.2 million), partially offset by a reduction in expectations for Disposal Facility Tax collections (\$500,000), and some minor net zero reclassifications between revenue categories (\$161,000) to more accurately reflect the revenues received from animal services activities.

The 2005-2006 Use of Money and Property

estimate was decreased by \$500,000 to reflect a reduction in the anticipated average cash balance for next year.

The 2005-2006 Revenue from Local Agencies estimate was decreased by \$1.3 million to reflect a recent downward adjustment to the calculation methodology for the Water Pollution Treatment Plant In-Lieu Fee (\$1.1 million), and a decrease (\$140,000) to reflect minor net zero reclassifications between revenue categories to more accurately reflect the revenues received from animal services activities.

The 2005-2006 Departmental Charges estimate was increased by \$299,000 to reflect minor net zero reclassifications between revenue categories (\$301,000) which more accurately reflected the revenues received from animal services activities, offset by minor reductions for lowered expectations related to Departmental fees and charges (\$2,000).

The 2005-2006 Other Revenue estimate was increased lowered by \$3.0 million to reflect the loss of State Jail Booking Fee reimbursements (\$2.5 million) included in the State Budget, and lowered expectations for Arena-related revenue (\$500,000), based on a more conservative presumption that the labor strife in the NHL would result in the cancellation of yet another season.

The Transfers and Reimbursements category was increased by \$3.5 million for 2005-2006, primarily as a result of technical adjustments. The overhead reimbursement increased by a net \$1.5 million to reimburse capital-related staff costs through the indirect cost allocation plan (overhead) methodology rather than by direct charge (this action was accompanied by increased General Fund costs), partially offset

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REVISED FORECAST BASE BUDGET (CONT'D.)

by a reduction in capital activity estimates that generated this revenue. The reimbursement from special and capital funds for their share of the operation and maintenance costs of the New City Hall (\$2.0 million) was also reflected along with a small decrease to the estimated proceeds from the Municipal Water System Rate of Return (\$5,000).

Revisions to the February forecasted 2005-2006 expenditure levels included a net zero technical adjustment increasing expenditures in the General Fund by \$3.02 million, to reflect a decision to account for capital-related support staff through the indirect cost allocation plan (overhead) methodology rather than directly charging the capital programs as discussed above. These adjustments affect the City Manager's Office (CIP Action Team and Budget Office Staff), Information Technology Department (Technology Customer Support and Strategic Planning) and Finance Department (Financial Transactions).

As a result of the same State action that eliminated the City's Jail Booking Fee reimbursement, Santa Clara County was to reduce by one-half (\$1.27 million), the amount that it bills the City for its share of jail booking costs. As a result, the 2005-2006 base budget allocation for this payment to Santa Clara County was reduced by that amount.

The cost increases to the City to maintain and operate the New City Hall were carried in the

February Forecast as a net number (with the cost increase required reduced by the amount of reimbursement estimated to be received). In the Forecast Base Budget, a net zero technical adjustment to correctly allocate these costs and reimbursements was made that resulted in an increase in expenditures in the General Fund of \$3.4 million.

Finally a series of smaller adjustments resulted in miscellaneous savings of \$474,000.

PROPOSED BUDGET BALANCING STRATEGY

Specific City Council direction regarding the preparation of the Proposed Budget was provided in the Mayor's March Budget Message. The details of the specific elements of that Message and the responses contained in this budget are provided in Attachment B. Attachment C contains information regarding the status of City Auditor recommendations with funding impact.

As summarized in Table II and discussed below, the budget balancing strategy developed by the Administration resulted in a balanced 2005-2006 General Fund Proposed Budget totaling \$745.35 million. Following is a brief discussion of the key elements of the budget balancing actions that were included in that Proposed Budget. Much more detailed descriptions of these elements are provided elsewhere in that document, and in the 2005-2006 Proposed Fees and Charges document that was published in May.

General Fund Balancing Strategy Detail (Cont'd.)

PROPOSED BUDGET BALANCING STRATEGY (CONT'D.)

Table II
2005-2006 PROPOSED OPERATING BUDGET
General Fund Funding Requirements and Balancing Strategy

	2005-2006	Ongoing
Revised Forecast	(\$ 57,242)	(\$ 57,242)
Development Fee Program Impact	(810)	(810)
Revised Forecast	(\$ 58,052)	(\$ 58,052)
Balancing Strategy		
Additional Resources		
Available Fund Balance:		
2005-2006 Future Deficit Reserve	\$ 12,541	\$ 0
Economic Uncertainty Reserve	10,436	0
Enhanced Parks Maintenance Reserve	1,000	1,000
Development-Related Fee Program Reserves	434	0
Liquidation of Encumbrances	355	0
Transfers:		
Construction Excise Tax Fund	2,000	2,000
Cardroom Revenue	8,500	0
Business Tax Amnesty Program Revenue	1,000	0
Development-Related Fee Revenue	623	531
Other Revenue Changes	5,197	3,327
Subtotal Additional Resources	\$ 42,086	\$ 6,858
Funding Changes by City Service Area		
Aviation Services	\$ 0	\$ 0
Environmental & Utility Services	(43)	(43)
Economic & Neighborhood Development:		
Non-Development-Related Programs	(260)	(750)
Development-Related Fee Programs	237	159
Public Safety	(4,241)	(4,326)
Recreation & Cultural Services	(4,160)	(5,765)
Transportation Services	(2,997)	(2,802)
Strategic Support	(4,502)	(9,553)
Funding Changes by City Service Area	(\$ 15,966)	(\$ 23,080)
Total Balancing Strategy	\$ 58,052	\$ 29,938
Remaining Balance	\$ 0	(\$ 28,114)

General Fund Balancing Strategy Detail (Cont'd.)

PROPOSED BUDGET BALANCING STRATEGY (CONT'D.)

Additional Resources

A total of \$42.09 million in additional resources with an ongoing value of \$6.86 million was recommended as part of the City Manager's proposed balancing strategy. The major elements of this increase are described below.

Available Fund Balance

The Proposed Budget balancing strategy included the utilization of additional Unrestricted 2004-2005 Ending/2005-2006 Beginning Fund Balance in the amount of \$24.41 million. This increase resulted from three major actions.

The first portion of the fund balance increase reflected direction provided by the City Council through approval of the Mayor's March Budget Message to use two reserves to help address the projected 2005-2006 shortfall. In compliance with that direction, the Proposed Budget recommended the liquidation and utilization of the 2005-2006 Future Deficit Reserve (\$12.5 million), and the remaining balance of the Economic Uncertainty Reserve (\$10.4 million). Also included were the recommended uses of portions of the Public Works and Planning Fee Reserves to help resolve the shortfalls in those two cost-recovery fee programs (\$434,000).

A second element of the increased fund balance proposed the liquidation and use of a portion of a third reserve, the Enhanced Parks Maintenance Reserve in the amount of \$1.0 million for a three year period to help mitigate the necessity of making even deeper cuts to

Parks Maintenance services than were already proposed in this budget. This reserve totaled \$5.1 million.

Finally, a third increase in fund balance would result from a proposed increase of \$355,000 to the estimate for liquidation of prior year carryover encumbrances, reflecting additional savings from the City Attorney's Office (\$166,000), and the Office of the City Manager (\$189,000) proposed as part of those office's reduction plans.

Transfers

A \$2.0 million transfer from the Construction Excise Tax Fund (a general purpose fund) was proposed to assist in decreasing the General Fund shortfall. This would be the third straight year that funds would have been diverted from the Traffic Capital Program for budget balancing purposes, which, of course, reduces the amount of funding available for traffic capital improvements.

Cardroom Revenue

In accordance with City Council direction to phase out the City's ongoing reliance on cardroom revenue, as of 2005-2006 all of this revenue (\$8.5 million this year) will have been removed from the Base Budget Forecast and reserved for one-time uses. The Proposed Budget again recommended the use of these funds as a one-time balancing action to help resolve the 2005-2006 General Fund shortfall.

Business Tax Amnesty Program Revenue

Consistent with the Mayor's Message, the Proposed Budget included a recommendation that the City conduct a Business Tax Amnesty Program for the payment of delinquent business tax. The program would waive penalties and interest otherwise due, serving as a mechanism to identify and collect on

General Fund Balancing Strategy Detail (Cont'd.)

PROPOSED BUDGET BALANCING STRATEGY (CONT'D.)

Additional Resources (Cont'd.)

Business Tax Amnesty Program Revenue (Cont'd.)

delinquent business taxes. The program is expected to generate one-time revenue of \$1.0 million in 2005-2006.

Development-Related Fee Revenue

Changes in development-related fee revenue estimates are expected to generate an additional \$623,000. The major components of this increase are adjustments to the Building and Fire Fee Programs. The revenue estimate for the Building Fee Program reflects an increase of \$374,000 based on anticipated activity. There were no fee increases proposed in this area. The Fire Fee Program revenue is expected to increase by \$283,000 as the result of restructuring fees in that program to an hourly basis and establishing new fees for services provided.

Other Revenue Changes

Additional revenue of approximately \$5.2 million was recommended to be added in this category, resulting from a series of specific proposals including: fee increases, economic development related grant reimbursements, telecommunications contract management reimbursements, as well as transfers and reimbursements from other funds and agencies. Revenue increases also resulted from changes to overhead reimbursements and an increase in reimbursements from the Redevelopment Agency.

Proposed Budget Funding Changes by City Service Area

The remainder of the balancing strategy involved a multitude of specific proposed expenditure actions, resulting in a net reduction of \$16.0 million, with an ongoing value of \$23.1 million. These reductions bring with them a variety of negative service level impacts.

A listing of the proposed budget modifications is provided by City Service Area (CSA) in Table II and all of the proposals are described in greater detail in the CSA and departmental sections of this document.

ADOPTED BUDGET BALANCING STRATEGY

The final phase of the 2005-2006 budget process commenced following the issuance of the City Manager's Proposed Budget document and consisted of the following major steps: review by the Mayor and City Council Budget Study Sessions of the Proposed Budget; issuance by Administration of recommended revisions to the Proposed Budget (in the form of formal Manager's Budget Addendums, or MBA's); formal public input through the Public Hearings process; issuance of the Mayor's June Budget Message memorandum; and approval by the City of a final Adopted Budget. A significant number of revisions to the Proposed Budget occurred in this final phase of the process and are described below.

Summarized in Table III by general category are the additional funding requirements introduced by Manager's Budget Addendums or the Mayor's June Budget Message. (Full

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ADOPTED BUDGET BALANCING STRATEGY (CONT'D.)

text of the Message is included as an Appendix to this document.) Those additional requirements totaled \$96.3 million. By far the largest component of the increase

was rebudgets of 2004-2005 funds (\$92.9 million) to be carried forward for the completion of various projects. Detailed descriptions of the approved changes and are provided in the specific City Service area sections of this document.

Table III
2005-2006 ADOPTED OPERATING BUDGET
General Fund Funding Requirements and Balancing Strategy

	2005-2006	Ongoing
Remaining Balance (from Table II)	\$ 0	(\$ 28,114)
Balancing Strategy		
Additional Resources		
Fund Balance to Support 2004-2005 Projects	\$ 72,145	\$ 0
Transfers:		
Construction Excise Tax Fund	500	500
Construction and Conveyance Tax Fund	1,000	0
Storm Sewer Operating Fund	102	102
Augmentation-Related Revenue	1,557	93
Other Revenue Changes	<u>21,034</u>	<u>0</u>
Subtotal Additional Resources	\$ 96,338	\$ 695
Funding Changes by City Service Area		
Public Safety	\$ 3,715	\$ 3,668
Recreation & Cultural Services	2,601	964
Economic & Neighborhood Development:	250	0
Transportation Services	(609)	(527)
Strategic Support	(2,478)	(303)
Other Funding Changes::		
Rebudgeted 2004-2005 Projects	<u>92,859</u>	<u>0</u>
Funding Changes by City Service Area	\$ 96,338	\$ 3,802
Total Balancing Strategy	\$ 0	\$ 3,107
Remaining Balance	\$ 0	(\$ 31,221)

General Fund Balancing Strategy Detail (Cont'd.)

ADOPTED BUDGET BALANCING STRATEGY (CONT'D.)

Additional Resources

As part of the City Council-approved revisions to the Proposed Budget, a total of \$96.3 million in additional resources were approved to be utilized as part of the Adopted Budget strategy. The major elements of these revisions are described below.

Fund Balance to Support 2004-2005 Projects

The unrestricted portion of the 2004-2005 Ending/2005-2006 Beginning Fund Balance estimated was adjusted upward from earlier estimates by an additional \$72.1 million to reflect the 2004-2005 funding which is estimated to be available to be carried over to 2005-2006 to complete previously approved projects.

Transfers

Three transfers were approved to assist in decreasing the General Fund shortfall: \$1.0 million from the Construction and Conveyance Tax Fund (excess tax funds collected in 2004-2005); \$0.5 million from the Construction Excise Tax Fund (to assist in decreasing the General Fund shortfall); and \$102,000 from the Storm Sewer Operating Fund (payment for renting office space at the old Martin Luther King, Jr library).

Augmentation-Related Revenue

Actions resulting in a net increase of \$1.6 million were approved. This increase recognizes the receipt of federal and State grants in the Police and Parks, Recreation and Neighborhood Services Departments for public safety and youth related activities and increased income from departmental charges for the Young People's Theater.

Other Revenue Changes

Reimbursements from various local, State and federal grant programs, which were awarded but not received in 2004-2005, were reflected along with corresponding budget changes. This included various public safety and neighborhood and literacy activities.

Adopted Budget Funding Changes by City Service Area

Actions resulting in a net addition of \$96.3 million were approved as part of the Adopted Budget phase. The following highlights some of the more significant General Fund budget changes that were approved in the final phase of the process and have been grouped by City Service Area.

Public Safety

Funding of \$3.7 million was included for restoration of Challenges and Choices (\$575,657), Crime Prevention Programs (\$1,093,130) (such as Neighborhood Action and Neighborhood Watch), Truancy Abatement (\$231,415), Police Investigations staffing (\$562,771), Police Training and Support services (\$185,252), Fire Apparatus staffing for the water tender and hose wagon (\$697,147); equipment for the Sex Offender Enforcement Team (\$25,000); and various Public Safety Grants (\$344,391).

Recreation and Cultural Services

Funding was approved for partial restoration of Library hours and services along with the addition of Sunday hours at seven geographically-distributed branch libraries (\$800,000) and operating subsidy to History San José (\$25,000); full restoration of funding for Arena Green and operation of the carousel (\$104,051), Young People's Theater

General Fund Balancing Strategy Detail (Cont'd.)

ADOPTED BUDGET BALANCING STRATEGY (CONT'D.)

Additional Resources (Cont'd.)

Recreation and Cultural Services (Cont'd.)

(\$92,696), and support of the Washington Youth Center (\$35,066); repair of the Mayfair pool (\$379,000); and elimination of City support for the Silicon Valley Football Classic (-\$100,000), which was decertified by the NCAA and various literacy activity grants (\$1,265,000).

Economic and Neighborhood Development

One-time funding in the amount of \$250,000 for the establishment of a Sports Opportunity Fund was approved. Usage of the fund will be presented to the City Council for discussion and possible approval.

Transportation Services

Partially offsetting restorations in other areas were the approved reductions in three areas in Transportation Services: Streetlight Operations (turning off approximately 10% of the street lights in the City saving \$320,000 in 2005-2006), New Infrastructure Assets Maintenance (eliminated funding provided in Tier 1 for maintenance expenses related to new transportation infrastructure assets that will become operational in 2005-2006 saving \$221,000 in 2005-2006); and further reduction to the sidewalk repair grant program (fewer homeowners who occupy their own homes will receive reimbursement for the repair of their sidewalks for a savings of \$67,489 in 2005-2006).

Strategic Support

One-time funding in the amount of \$50,000 was approved for the City Clerk to monitor

the new reporting requirements under the new ethics ordinance changes. Offsetting this increase were adjustments in three Strategic Support activities. They include the one-time elimination of the transfer to the Vehicle Fund for the replacement of General Fleet vehicles, this represents the fourth consecutive year in which no funds are budgeted for the replacement of vehicles in the general fleet for a savings of \$1,750,000 (included in the proposed budget was an ongoing reduction of \$1.0 million); elimination of the Employee Parking Payment to the City's Parking Fund saving \$500,000 (included in the proposed budget was a reduction of \$115,600); and in implementing the final Interim Space Use Plan for Existing City Facilities savings of \$352,958 will be realized.

Other Funding Changes

Funding for completion of programs and projects authorized in the prior year was approved. The largest majority of the rebudgets occurred in three areas: Capital (\$10.7 million), Earmarked Reserves (\$43.3 million) and City-Wide Expenses (\$34.9 million).

Future Implications

As shown on Table III and mentioned above, a total of \$31.2 in one-time solutions were approved as part of the strategy to balance this budget.

The most recent projections for the 2006-2007 General Fund status (as shown in the recent Five-Year Forecast document) was for a shortfall of approximately \$32.1 million that year. Assuming the basic assumptions utilized in that forecast were close to being correct, the carryover impact of the one-time measures contained in this budget would lead to an increase in the estimate for a 2006-2007 shortfall to approximately \$63 million.